Bell Atlantic made the following assumptions about reducing future benefit costs:[42]

1. Both management and associate retirees' future Medicare Part B reimbursement amounts were frozen at the 1991 Part B amount.

2. Certain future dental claim payments to dentists would be reimbursed based on current maximum dollar amounts per current fee schedules. These amounts vary by type of service.

3. Future management retirees were assumed to share in the cost of postretirement health coverage. For management retirements after 1991, cost sharing amounts vary with respect to medical coverage for the retiree, the first dependent and all other dependents, and by calendar year. Retirees would share in cost increases over 1993 projected claims cost for their own coverage. First dependents would pay 50% of the average claims cost phased in over 20 years. Additional dependents would pay 100% also phased in over 20 years.

4. Future associate retirees were assumed to share in the cost of postretirement health coverage. Associates who retired after 1989 were assumed to share in the cost of medical coverage beginning in 1993. The sharing amount depended on whether the retiree is younger than 65 years or older than 64 years, and whether the retiree was single or has a family.

14. Adjustments to Exogenous Costs to Avoid GNP-PI Double Counting.

The Godwins Study calculated the impact of SFAS 106 on GNP-PI. This study was performed in 2 stages: (1) Actuarial Analysis and (2) Macroeconomic Analysis. The Actuarial Analysis compared SFAS-106 costs for Price Cap LECs to those an average employer will experience. The Macroeconomic Analysis determined the impact of SFAS 106 on GNP-PI. These analyses incorporated the effect the growth in medical costs

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42 See also information provided in paragraph 12, above.

will have on GNP-PI. Therefore no further adjustment is needed to avoid double counting.[43]

The Godwins Study determined that SFAS 106 costs would ultimately increase the GNP-PI by 0.0124%, which included the growth in medical costs. This increase is not likely to happen immediately, but to be conservative, Bell Atlantic reflected the eventual impact on GNP-PI in the first year that there could possibly be any impact.

The Godwins Study also identified a possible reduction of 0.93% in the average wage rate in the economy as a result of SFAS-106. This eventual wage reduction would affect all employers including Price Cap LECs. Any wage reductions would eventually have a downward pressure on GNP-PI and, therefore, will be reflected in rates.[44]

Moreover, decreases in wage rates are by definition endogenous. Companies have some degree of control over the wages paid to their employees. As a result, no adjustment for

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[43] The growth in medical costs is likely to have a significantly greater impact on Price Cap LECs than on the average employer for the reasons discussed above. Bell Atlantic does not propose that there should be an adjustment to the Price Cap formula to reflect this risk. The exogenous event is not the providing of postretirement benefits, but the change of accounting for these benefits.

[44] The majority of Price Cap LECs' wages are determined based on bargaining agreements. Therefore, it will be harder for Price Cap LECs to achieve these wage reductions. Price Cap LECs also are capital intensive businesses. Compared to the average employer, therefore, wages are a smaller percentage of total costs. As a result, the average employer is likely to benefit more from the drop in the national average wage rate than are the Price Cap LECs.

this endogenous item should be made in determining the amount of SFAS 106 costs to be given exogenous treatment.[45]

15. Description and Documentation of Macroeconomic Model Used in the USTA Study.

Attached to this direct case is Bell Atlantic's Transmittal No. 497, which included the Godwins Study. The Godwins Study describes the method of estimation, parameter estimates, and summary statistics, and includes sensitivity analyses. Godwins has also provided additional information on the macroeconomic model and its calibration. Attachment E is the additional information provided by Godwins.

CONCLUSION

Bell Atlantic has demonstrated that the costs resulting from SFAS 106 are exogenous, and has filed with the Commission tariffs

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[45] For example, if Bell Atlantic increases wages this year, Bell Atlantic could not receive exogenous treatment for these wage increases. Conversely, if Bell Atlantic decreases wages, this decrease would increase productivity. If Bell Atlantic achieves a productivity gain that results in Bell Atlantic earning greater than 12.25% rate of return, Bell Atlantic is required to share with customers a portion of this productivity gain.

appropriately reflecting those costs. The Commission should approve Bell Atlantic's tariffs.

Respectfully submitted,
The Bell Atlantic Telephone Companies

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June 1, 1992

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing "Direct Case of Bell Atlantic" was served this 1st day of June, 1992, by delivery thereof by first class mail, postage prepaid, to the parties on the attached list. An asterisk (*) indicates that the attachments to this document have been served upon the parties so designated under seperate cover.

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ATTACHMENT A

Duff & Phelps Inc.

CREDIT DECISIONS

Volume 9 Number 11 March 23, 1992

SFAS 106 And Its Impact On Utility Credit Quality

In December 1990, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" or "PBOPs." SFAS 106 applies to all PBOPs but focuses primarily on health care. The FASB considers that PBOPs should receive the same recognition as a pension commitment.

Although the liability has always existed, a disclosure in utility financial statements will shed a much brighter light on this item by 1993. SFAS 106 must be adopted no later than fiscal years beginning after December 15, 1992. Utilities are in the situation, unlike other companies, of having to recover PBOPs costs in rates. Therefore, the credit quality may be either positively or negatively affected depending on each utility's regulatory support.

What Is SFAS 106?

Although the FASB wants PBOPs treated like pension benefits, medical costs are less predictable and increasing much faster than the wages which dictate pension payments. The characteristics of the workforce or low employee turnover in some industries could add to companies' financial burden. In an attempt to lower costs, utilities and other companies are looking at ways to shift more of the burden onto employees and retirees by capping benefit contributions, or by offering employees various plans for them to accumulate funds to meet retirement medical costs. Some companies have terminated medical coverage for new retirees.

Because utilities have unionized workers, a revised benefits package has to be part of contract negotiations. Company sponsored retiree medical coverage may be eliminated for more employees, particularly as there are changes in national health care policy.

While SFAS 106 provides for liability recognition, funding for the liability remains a question. The various funding plans being studied for health care coverage include Voluntary Employees Beneficiary Association (VEBA) and other tax advantaged 501(c) trusts, 401(h) accounts, and corporate-owned life insurance. Nonetheless, the ability to fund the PBOPs liability on a tax-advantaged basis, similar to pensions, currently appears to be limited.

The new accounting standard requires that the utility adopt the accrual method to establish a reserve for PBOPs costs incurred for participants' prior benefits. The employer must fully accrue an employee's PBOPs obligation before the employee is eligible to receive these benefits. Companies will be required to disclose the expected PBOPs obligation based on the present value of anticipated benefit payments to be paid to employees after retirement. Utilities, and most other companies, currently recognize these costs only on a cash, or "pay-as-you-go," basis as claims are actually paid for the retired employee.

When a company adopts SFAS 106, it must then book a liability calculated as the present value of all future PBOPs accrued and unfunded for retired and current employees. SFAS 106 proposes to allow this accrued benefit obligation, or "transition obligation," to be booked immediately or amortized over the shorter of the average remaining service period of current employees or 20 years. Cash outlays for postretirement benefits will not change, but the annual expense to be recognized for financial reporting purposes will increase.

Utility Regulation and SFAS 106

For utilities, the impact of SFAS 106 on financial results will depend on regulatory treatment. Following are the three potential regulatory scenarios:

(1) The preferred option is approval to recover the accrued costs in current rates and contribute

(Cont. on Page 6)

Also In This Issue . . . Page

LATEST RATING ACTIONS

As we went to press with this issue, the following rating actions were taken; more details will be provided in a future issue of *Credit Decisions*.

Rating Changes

Company	Rating Action	Security Class	From	To
Gulf States Utilities Co.	Upgrade	FMB Pfd. Stock	BBB- DP	BBB BB+

New Ratings/New Issues/Rating Watch/Reaffirmation/Withdrawal

Company	Rating Action	Security Class	Rating
BankAmerica Corp.	New Issue	Notes	A
Boatmen's Bancshares, Inc.	Rating Watch—Unfavorable	Sub. Debt	A-
Boatmen's National Bank of St. Louis	Rating Watch—Unfavorable	Long-Term CDs	A+
Citicorp	New Issue	Pfd. Stock	BBB-
Delta Air Lines	New Issue	Notes/Debs.	BBB
Gulf States Utilities Co.	New Rating Reaffirmation	Debs./PCRB (NCol.) Pfc. Stock	BBB- DP
Houston Lighting & Power	New Issue Reaffirmation	FMB/MTN Cum. Pfd. Stock (Shelf) FMB/Sec. MTN/PCRB (Col.) PCRB (NCol.)/Pfd. Stock Comm. Paper	A+ A A+ A Duff 1
Idaho Power Company	New Issue	FMB	A+
Procter & Gamble	New Issue	Notes	AA
Stone Container Corp.	New Issue	Sr. Sub. Notes	B+
Wisconsin Power & Light Co.	New Issue	F&RMB	AA

FIXED INCOME UPDATE

Following is a compilation of recent developments. The event may cause a changing trend in risk but it would not be outside the range satisfactory for the current D&P rating. Further, the implication is not necessarily sufficient to warrant a Rating Watch addition.

Company	Rating	Implication
Arkansas Power & Light	**BBB**	**Expected**
Union Electric	**A+**	**Expected**

Union Electric completed purchase of AP&L's Missouri properties. The transaction, valued at $63 million, will add approximately 26,000 customers to Union Electric's customer base.

Company	Rating	Implication
Black & Decker Corp.	**BB**	**Positive**

Black & Decker plans to raise $750-780 million to pay down a portion of its $2.6 billion of long term debt. In two offerings, Black & Decker will sell all of the stock in its information and service business: PRC Advanced Systems Inc. (for proceeds of $330-360 million) and offer 18 million common shares of its own stock (expected to raise about $420 million).

Company	Rating	Implication
Consolidated Edison of NY	**AA-**	**Positive**

The New York PSC approved in principle a three-year electric rate settlement reached in January with the Commission staff. The PSC sent the plan back to the parties with certain modifications made by the Commission, including one to levelize the rate increases for the term of the plan. The settlement authorizes revenue increases and adjustment and incentive mechanisms that, if accomplished, would permit returns of up to 12% on equity. The equity ratio would be raised to 52%, an important positive. The settlement includes an electric revenue adjustment mechanism (ERAM) which would remove earnings effects of variability in weather and sales forecasts.

Company	Rating	Implication
Dayton Hudson Corp.	**A+**	**Positive**

DH will eliminate 630 positions (half are management posts) and close a Minneapolis and possibly a Detroit warehouse. These actions primarily affect employees at 19 Dayton's and 23 Marshall Field's stores, but will impact just 2% of DH's 34,000 employees.

Company	Rating	Implication
General Electric Company	**AA+**	**Negative**

The Justice Department charged GE with fraudulently diverting U.S. government funds earmarked for Israeli military jet engines to an Israeli general. In a suit recently amended in Cincinnati federal court, the amount of alleged fund diversion was raised to $40 million from the $30 million previously documented. GE said it has initiated disciplinary action against 20 top managers of its aircraft engine unit in connection with this case. Impact on future government contracting is uncertain at this time.

FIXED INCOME UPDATE (Cont.)

Company	Rating	Implication

Kansas Gas & Electric — **BBB+** — **Uncertain**
Kansas Power & Light — **AA-** — **Uncertain**
Merger of KP&L with KG&E has been delayed pending analysis of sounds heard at the Wolf Creek nuclear station of which KG&E has a 550 mw share. The merger had been scheduled to occur on March 16.

KeyCorp — **A-** — **Neutral**
KeyCorp will buy the $4.9 billion Puget Sound Bancorp in a $800 million stock swap. With this acquisition, KeyCorp will increase its market share in the Seattle/Tacoma Washington area to 8.3% from 1.3%, making it third largest. The new combined entity will be called Key Bank of Washington.

MCI Communications — **BBB+** — **Positive**
MCI has been awarded a 10-year contract valued at $558 million to provide air traffic control communications links to the FAA.

Pfizer Inc. — **AA** — **Negative**
The U.S. Food and Drug Administration asked Pfizer to warn recipients of its larger 60 degree Shiley heart valves that the risk of fracture is up to five times higher than previously estimated. An FDA official said that the fracture risk for its 23,000 U.S. and Canadian patients might be great enough to warrant replacing these valves in some individuals.

Public Service Co. of New Mexico — **BBB-** — **Positive**
PSNM signed a three-year agreement to sell power to Imperial Irrigation District of California. Under the agreement, PSNM will provide 56 mw of base demand year-round, and an additional 25 mw of seasonal demand from April through October.

Sierra Pacific Power — **A-** — **Positive**
Parent filed shelf for 1.5 million of common shares. A portion of proceeds are expected to be used for debt repayment and additional equity investment in its subsidiaries.

Southwestern Bell — **A+** — **Positive**
SWBT reached agreement with Communications Workers of America which would eliminate up to 1,000 jobs by year-end through early retirement offers to union employees. The jobs are part of the 2,000 identified by SWBT as surplus, more than half of which are expected to be eliminated through early retirement.

RATING UPGRADE

	Security Class	From	To	Mdy's/S&P	Fixed Obligation Ratio 1991E	Fixed Obligation Ratio 1992E	Fixed Charge Coverage 1991E	Fixed Charge Coverage 1992E
The Dayton Power & Light Company	FMB/PCRB (Col.)	BBB+	A+	A2/A	48%	48%	2.2X	2.5X
	Debs.	BBB+	A	A3/A-				
	Pfd. Stock	BBB	A	"a2"/A-				

We have raised the ratings of Dayton Power & Light Company's first mortgage bonds and collateralized pollution control revenue bonds to 'A+' from 'BBB+', debentures to 'A' from 'BBB+', and preferred stock to 'A' from 'BBB'. Dayton Power & Light's financial protection measures and cash flows are expected to improve significantly with the implementation of recent electric, gas, and steam rate settlements. The company was allowed to increase electric revenues approximately $129 million under a three-year phase-in plan to recover Zimmer costs. With the 1991 completion of the 1300 mw Zimmer coal plant (365 mw interest for Dayton), construction will return to more manageable levels. Spending will largely reflect the addition of new peaking capacity and demand side management programs. The company's acid rain requirements are minimal and will center on fuel-switching. Dayton Power & Light is a low-cost energy producer and has well-maintained, efficient plants. Management strategy has been effective in positioning the company for the risks the industry faces. Dayton Power & Light Company, the principal subsidiary of DPL Inc., provides electric, natural gas, and steam service in a 6,000 square mile area of west central Ohio.

RATING UPGRADE/NEW ISSUE

	Security Class	From	To	Mdy's/S&P
Massachusetts Municipal Wholesale Electric Company	Bonds	BB+	BBB+	Baa1/BBB

We have raised the rating of Massachusetts Municipal Wholesale Electric Company's (MMWEC) revenue and refunding bonds and non-defeased portions of 1981 Series B and 1982 Series A bonds to 'BBB+' from 'BB+'. The securities are removed from Rating Watch — Favorable. A rating of 'BBB+' is also assigned to MMWEC's proposed sale of $284 million of power supply system revenue bonds, the first installment of an expected $730 million ongoing refunding program. The refunding program will significantly lower MMWEC's debt service requirements. Substantial savings to members will result in more competitive rates. The legal status of the power sales agreements (PSAs) with its Massachusetts participants, which secure MMWEC's debt obligations, has been strengthened. A favorable Massachusetts Supreme Court decision in 1991 affirmed the validity of the Massachusetts' participants Project 6 power sales agreements with MMWEC and that MMWEC properly invoked the step-up provisions under these agreements. Appellant's petition for a writ of certiorari and other attempts to review the Massachusetts Supreme Court decision have been denied by the U.S. Supreme Court. There have also been favorable developments regarding the validity of the PSAs of the Massachusetts participants in the arbitration proceedings emanating from the Hull Municipal Lighting Plant litigation. Several of the remaining counts in the arbitration proceedings and some of the issues that may be addressed in any future litigation of the Massachusetts Supreme Court decision have been adjudicated in favor of MMWEC in other court proceedings. In upgrading MMWEC's rating, we relied upon the opinion of Bond Counsel (Mudge Rose), Bond Counsel's evaluation of the validity of the Massachusetts PSAs, and the assessment by MMWEC and counsel of the expected future favorable resolution of challenges to the validity of the PSAs. In its examination of all major litigation involving the PSAs, Bond Counsel did not find anything that would suggest that these obligations were not valid and binding upon the Massachusetts participants. Importantly, based on court opinions to date, opinions of counsel, and other considerations, MMWEC believes it is highly probable that it will be successful in defending against the rescission of the Massachusetts PSAs in response to outstanding claims.

RATING DOWNGRADE/RATING REAFFIRMATION

	Security Class	From	To	Mdy's/S&P	Debt Ratio		Pretax Interest Coverage	
					1991E	1992E	1991E	1992E
US WEST, Inc.	Cv. Sub. LYONs	A+	A	A3/A	50%	50%	2.9X	3.0X
US WEST Capital Funding, Inc.	Sr. Unsec. Debt	AA-	A+	A2/A+				
US WEST Communications, Inc.	Sr. Unsec. Debt.	-	AA	Aa3/AA-				
US WEST Financial Services, Inc.	Sr. Unsec. Debt	AA-	A+	A2/A+				

In addition to reaffirming the 'AA' rating of US WEST Communications, Inc.'s long-term senior unsecured debt and lowering the ratings of the non-regulated subsidiaries' long-term debt, we have reaffirmed the Duff 1+ commercial paper ratings of US WEST, Inc. and all of the above subsidiaries. These rating actions reflect the deterioration of US WEST's consolidated creditworthiness as a result of problems in US WEST's real estate operations. US WEST has been attempting to exit the real estate business and has established $400 million in reserves to cover anticipated losses during the liquidation period. US WEST, Inc. is directly or indirectly ultimately responsible for over $1 billion of real estate related debt. In addition, US WEST has agreed to support approximately $2.5 billion of US WEST Financial Services' debt and unconditionally guarantees the debt of US WEST Capital Funding, currently about $500 million. US WEST, Inc.'s LYONs, with a current accreted value of $400 million, are subordinate to all other debt of US WEST and its subsidiaries. The ratings also reflect the dividends US WEST receives from subsidiaries, principally US WEST Communications, that are available for support requirements and to honor guarantees. However operating subsidiaries' creditors have a prior claim on subsidiary earnings, dividends and assets.